THE DISTRIBUTION OF POWER TO REGULATE INTERSTATE CARRIERS BETWEEN THE NATION AND THE STATES

BY

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SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENTS
FOR THE DEGREE OF DOCTOR OF PHILOSOPHY
IN THE
FACULTY OF POLITICAL SCIENCE
COLUMBIA UNIVERSITY

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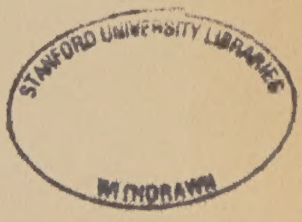

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1928

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My Father

FRANK REYNOLDS

PREFACE

In the study of transportation in the United States, economic and legal considerations are inextricably commingled. The economist and the lawyer are mutually dependent upon each other's services in their attempts to solve the problems which confront them in the transportation industry.

Transportation in most of its aspects is a highly regulated industry. The economist cannot analyze existing conditions in this industry nor venture predictions concerning its future without giving careful attention to the influences of state and federal regulation. In weighing the effects of regulation, he finds that its character and scope are determined, not only by legislative considerations of expediency, but also by legal restraints upon legislative power. The validity of regulatory legislation is decided by the courts. The history of the regulation of transportation cannot omit the prominent role played by the courts, and in attempting to improve existing conditions the attitude of the courts toward every proposed change in regulatory policy must be considered. Therefore, the economist must have some knowledge of the legal principles applicable to legislative power when he interprets the present status of the regulation of transportation and when he proposes changes therein. Furthermore, he is vitally interested in the transportation industry as a source of public revenues. From the standpoint of the amount of taxes paid by that industry, its property investment and its earning capacity, it occupies a very prominent place in the study of taxation. Here also attention must be given to legal considerations. Many taxes

levied upon transportation and its agencies have been declared by the courts to be invalid as exceeding the constitutional powers of the branch of government imposing the tax. Therefore, it is hazardous to analyze our present system of taxation or to propose changes therein without a very definite knowledge of the legal principles which determine the power of the taxing authorities.

On the other hand, the lawyer cannot hope to solve the legal problems concerning the powers of the state and federal governments to regulate or to tax the transportation industry without some knowledge of economic fact and theory. The decisions of the courts show a growing appreciation of the difficulty of deciding constitutional questions of legislative power solely upon the basis of abstract legal theory. The day is past in which the lawyer, preparing a brief on the validity of regulation or taxation, can safely confine his research to constitutions, statutes, court decisions and legal treatises. He must study and present to the court the economic facts upon which the demand for government action is based, and must attempt to analyze the economic consequences, favorable and unfavorable, which are likely to result therefrom.

This interdependence of law and economics is particularly apparent in studying the distribution between the state and the federal governments of the power to regulate or affect carriers engaged in interstate transportation. The way in which this power has been distributed by the United States Constitution, federal statutes, and judicial interpretation thereof, has largely determined the character of the regulation and taxation of such carriers. The economic consequences are vital. This may be shown by two important illustrations. At the close of the World War there was a grave question whether efficient interstate railroad transportation could be furnished under private management. The

railroad facilities were not physically adequate to provide prompt transportation for the volume of traffic that was offered, and the ability of the railroads to finance the enlargement of these facilities was seriously impaired by their failure to earn a return upon their investment sufficient to attract capital. At this juncture federal power was exercised to increase, not only the revenue derived from interstate transportation, but also that derived from traffic which did not cross state lines. This immediately raised the legal question of federal power thus to regulate intrastate transactions. If the United States Supreme Court had not sustained this exercise of federal power, it is very doubtful whether the railroads could have rehabilitated their financial position as they have done during the past seven years. A continuation of impaired credit and inadequate service would probably have aroused an acute agitation for government ownership and operation of interstate railroads. The other illustration is taken from the field of taxation. The argument was made that state taxation of property used in interstate transportation and of the net earnings derived from such transportation is illegal because it imposes a burden upon interstate commerce. If this argument had been sustained by the Court, the states and the various subdivisions thereof would have been deprived of a source of revenue from which they now derive a quarter of a billion dollars annually. The exemption of interstate railroad property and income from state taxing power would have had almost revolutionary effects upon our system of public finance. On the other hand, the distribution of power has to a large extent been determined by economic considerations. The same two illustrations may be used to show that this is true. Federal power to regulate the general level of intrastate rates was exercised and sustained largely because of the economic fact that an additional dollar earned from intra-

state traffic has just as much effect upon the credit of a railroad and its capacity to provide transportation facilities as an additional dollar earned from interstate traffic. The decisions sustaining state power to tax property used in interstate transportation and the net earnings derived therefrom were largely influenced by the Court's belief that, as a matter of economic fact, no serious impediment or restraint was imposed upon interstate commerce by compelling the industry of interstate transportation to contribute on equal terms with other taxpayers to the expenses of administering state governments.

The purpose of this discussion is to show how the control of carriers engaged in interstate transportation is divided between the state and the federal governments and to trace the process of judicial interpretation and legislative activity by which the present distribution of powers has gradually evolved from the provisions of the United States Constitution. In attempting to accomplish this purpose it is necessary to give a detailed analysis of many decisions of the United States Supreme Court because it is impossible to interpret the history of the distribution of powers or to make definite statements concerning the existing status without some knowledge and appreciation of technical distinctions made by the Court. The legal material here presented has, however, a direct bearing upon the work of the economist. It forms an important part of the history of transportation in the United States because the character of our past and present plans of regulation and taxation of interstate carriers has been largely determined by constitutional considerations. Furthermore, the economist is vitally concerned with the relation of state and federal powers in all his efforts to improve our transportation system. If he suggests legislative remedies, he must either coordinate his proposals with the present division of control between the states and the

nation or must embody in his legislative program measures to readjust the distribution of power within constitutional limits. Therefore, it is hoped that students of the economics of transportation will find some value in this statement and explanation of the legal foundation upon which our system of control of interstate carriers is based, and in the suggestion of many points of contact between the law and the economics of transportation.

Grateful acknowledgment must be made to Professor Thomas Reed Powell for suggesting the basis of much of the analysis of constitutional interpretation presented in this volume. When Professor Powell was a member of the Faculty of Political Science at Columbia University, I had the privilege of attending his lectures on Constitutional Law. The preparation of this study was commenced almost immediately thereafter, and these lectures provided an invaluable foundation for my approach to the many decisions herein discussed. I am deeply indebted to my teacher and friend, Professor Edwin R. A. Seligman, for his interest and helpful advice as the work progressed. I wish especially to thank Professor Noel T. Dowling and Dr. Robert L. Hale, both of whom read my manuscript with great care. Their criticism has enabled me, not only to eliminate many errors, but also to clarify and strengthen parts of the discussion which were far from satisfactory as originally written. To many others, whose work has been of great assistance to me and whose ideas are embodied in this volume, I have endeavored to make appropriate acknowledgment in the text.

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TABLE OF CONTENTS

PAGE

INTRODUCTION

Necessity for distribution of power 21
Role of Supreme Court and Congress in determining distribution 22
Outline of discussion 24

CHAPTER I

THE CONSTITUTIONAL GRANT OF FEDERAL POWER

Federal and state commerce powers under the Articles of Confederation ... 27
Defects of federal commerce power contributed to failure of Confederation. 29
Objects in view in framing the provisions of the Constitution concerning commerce 36
The provisions stated 38
No intention to restrict federal power to specific forms of regulation 40
No intention to grant unlimited federal power 43
Federal power to construct roads and canals not recognized by early statesmen 44
Intention of framers must be sought in Constitution itself 51
Exclusive federal commerce power not intended 52
Necessity for interpretative decisions 55
No express federal power to regulate intrastate commerce 56
Summary 57

CHAPTER II

JUDICIAL INTERPRETATION OF FEDERAL AND STATE POWERS. 1789–1887

Division of discussion by periods 59
Questions in interpreting commerce clause 59
Federal power 61
Definition of terms of commerce clause. *Gibbons* v. *Ogden* 61
Transportation by water 63
Transportation by land 65
Navigable waters of the United States. *The Daniel Ball* 67
Agencies of interstate transportation 68
Includes instrumentalities unknown when Constitution was adopted ... 69

PAGE

Federal power (*continued*)
Rates for interstate transportation 70
The "necessary and proper" clause. *McCulloch* v. *Maryland* 71
Intrastate commerce 74
Creation of corporations to construct and operate interstate railroads .. 75
State power 76
Concurrent state power *versus* exclusive federal power 79
The compromise. *Cooley* v. *Board of Wardens* 85
State power concurrent unless uniformity of regulation is necessary 85
Determination of need for uniformity 87
Interstate transportation requires uniform regulation 89
Exceptions 90
Police power 91
Inapplicable to interstate railroad rates 93
To exact compensation for privileges and facilities 96
To facilitate movement of interstate commerce 99
Taxing power 100
Limitations upon 100
Operations of agencies of United States government 101
Property of agencies of United States government 101
Property of United States 103
Interstate transportation 104
Property used in interstate transportation 104
Interstate passengers and freight 105
Corporations engaged in interstate commerce 107
Summary of judicial interpretation. 1789–1887 112

CHAPTER III

Judicial Interpretation of Federal and State Powers. 1887–1920

Introductory 117
Federal power 118
Terms of commerce clause re-defined 118
Charges for interstate transportation 120
Liability for loss or damage to interstate shipments 121
Physical instrumentalities of interstate transportation 122
Carriers engaged in interstate commerce 123
The Sherman Anti-Trust Law 124
The commodities clause 125
Relations between interstate carriers and their employees 128
Liability for death or injury 128
Hours of service 129
Membership in labor unions 130
Wages 132